Cost cutting was only the first step in transforming Tata Motors from a cyclical manufacturing company into a diversified powerhouse.

Leading change: An interview with the managing director of Tata Motors

Gautam Kumra

The transformation of Tata Motors into a highly successful, well-diversified, and globally ambitious automobile giant represents one of India's most remarkable corporate-success stories in recent times.

Six years ago, after a decade of strong revenue and margin growth, Tata Motors plunged into an unprecedented crisis when demand for its trucks suddenly collapsed. The lost sales—compounded by heavy investment for its entry into the passenger car business, the cost of complying with new emissions standards, and an increasing threat from overseas competitors—caused Tata Motors to shock the markets with a 5 billion rupee ($110 million) loss for the fiscal year ending March 2001.

Drastic action was required. Over the next two years, the company shaved around 8 billion rupees from its cost base and nursed itself back to corporate health. Even while keeping a tight grip on costs, Tata Motors moved to the offensive by refocusing its investments on less cyclical products, including light commercial vehicles, buses, and spare parts; making a successful entry into passenger cars; and responding to opportunities presented by favorable social and economic trends. These included the new mobility of young Indians, the government's substantial road-building program, and generally buoyant GDP growth.

Today Tata Motors ranks as the world's fifth-largest manufacturer of medium and heavy trucks—it has a 61 percent domestic market share in this segment—and has taken the number-two position for sales of passenger vehicles in the Indian market. It has also built a significant global presence, both through sales efforts in overseas markets (such as the former Soviet republics, the Middle East, South Africa, South Asia, and Turkey) and through acquisitions such as the takeover of Daewoo's commercial-vehicle business in South Korea and the purchase of a 21 percent stake in the Spanish bus manufacturer Hispano Carrocera. In addition, Tata Motors has formed a joint venture with Marcopolo, the Brazilian bus manufacturer. With an agreement in early 2006 to distribute Fiat cars in the Indian market and a more recent memorandum of understanding with Fiat to establish a joint manufacturing facility near the Indian city of Pune, Tata Motors has embarked on a wide-ranging global partnership with the Italian group—an arrangement that both sides expect to flourish.

Ravi Kant, the managing director of Tata Motors and former head of the company's commercial-vehicle business, recently met with McKinsey director Gautam Kumra. In this interview, Kant told Kumra about some of the key lessons of the transformation.

McKinsey: *Can you start by describing the impact on the company of the 2001 crisis—and what caused it?*

Ravi Kant: Seven years ago, Tata Motors was predominantly a manufacturer of commercial vehicles, and that is a very cyclical business. At the time, we were making huge investments in car manufacturing to move away from that cyclicality. But while we were in the middle of this diversification, the commercial-vehicle market in India shrank by more than 40 percent, with massive consequences for both the top and, more particularly, the bottom lines of the company. The 5 billion rupee loss in 2001 was the first time something on this scale had happened in the company's history, and it really shook everybody within the organization. In my experience, you either get knocked over by something like this or you do something about it. Our reaction was to try to understand what had gone wrong and to create a path for the future to ensure that we never got into such a situation again. The good news, at least, was that we still retained our leadership position and our market share, albeit in a much smaller market. So in 2001 we decided on a recovery strategy that had three distinct phases, each of which was intended to last for around two years—six years in all.

McKinsey: *How did you characterize the main theme of these three phases?*

Ravi Kant: Phase one was intended to stem the bleeding, since we just couldn't ignore the fact that our sales volumes were still falling with the shrinkage of the overall market. Costs had to be reduced in a big way, and that was going to be a huge challenge for a company that was not only the market leader but had been used to operating in a seller's market and employing a cost-plus approach to pricing. Phase two was to be about consolidating our position in India, and phase three was to involve going outside India and expanding our operations internationally.

McKinsey: *What were the main achievements of the first phase?*

Ravi Kant: The key objectives were to move to a system of market pricing and to reduce our break-even point, both of which called for major reductions in costs—variable costs, fixed costs, and interest costs. We used many approaches to cost reduction, including benchmarking our rivals. For example, we took apart vehicles to see what we could do to modify our products and to lower costs. We went in for e-sourcing, which was then very new, but today we are the largest

Vital statistics
Born June 1, 1944, in Balia, India

Married with 2 daughters

Education
Attended Mayo College, Ajmer; graduated in 1966 with BS in technology from Indian Institute of Technology, Kharagpur

Earned MS in engineering management in 1970 from Aston University in Birmingham, United Kingdom

Career highlights
Tata Motors
- Managing director (2005–present)
- Executive director, commercial-vehicle business unit (2000–04)

Philips (1998–99)
- Director, consumer electronics, India

LML (1991–98)
- Senior executive director

Titan Industries (1986–91)
- Senior executive director

Fast facts
Serves on governing board of National Institute of Design and as vice president of Society of Indian Automobile Manufacturers

Served as chairman of Audit Bureau of Circulations, India; Advertising Standards Council of India; National Readership Studies Council

Ravi Kant

company doing e-sourcing in India and one of the leading ones in the automobile industry worldwide. In two and a half years, we reduced our break-even from nearly two-thirds of capacity utilization to around one-third, which meant that even if the market shrank by close to 60 percent, we would still be in the black. The whole organization really got together to ensure that the bleeding stopped.

McKinsey: *It's clear that the second and third phases of the transformation—domestic consolidation and overseas expansion—have restored the health of Tata Motors and reignited top-line growth. Did you simultaneously plan for these during the first phase?*

Ravi Kant: Absolutely. The concentration in phase one was indeed on cost reduction, but while this was going on we had to think about taking action in areas that would have an impact during the other phases. For phase two, the concentration was on improving product quality and upgrading product features so as to make the products more competitive. We also started work on new products that would be required by the market after three to five years and strengthened our position in the marketplace by setting up a new sales-planning process, tightening credit norms, improving the liquidity and profitability of the dealers, reorienting toward customer satisfaction, and extending the reach of our distribution network. For phase three, the concentration was on starting work on international markets by identifying key markets and segments and developing a comprehensive plan to improve our competitive position so as to get a respectable market share. We also started looking at opportunities for inorganic growth.

McKinsey: *What sort of opposition did you encounter generally to the cost reduction phase? And how did you deal with it?*

Ravi Kant: I certainly learned that the wisest approach is not to give orders but to sell new ideas internally. Generally, people with greater experience, especially in a successful company, are often resistant to change because they have been successful doing things the way they have been used to, not realizing that the context has changed. This process of selling new ideas took longer, of course, but unless people are convinced about what you are asking them to do, they are not going to make it happen. Therefore, one had to keep reasoning and get people to come to their own conclusions. When you force people to confront the issues themselves, most of them realize that there is actually no other option; you have to do it in the manner suggested. But when you are used to doing things in a certain manner, it takes a long time to orient yourself to a different way. That's entirely human.

'The most effective way to sustain change is to make those involved internalize it rather than just getting somebody to come and talk about it'

Our people are very dedicated, but the organization had become very inward looking. The trick was how to expose people to the outside world to allow them to see what is happening there rather than drilling change into them through speeches and letters. We felt that would be very artificial and would upset intelligent people. The most effective way to sustain change is to make those involved internalize it rather than just getting somebody to come and talk about it. For example, we had our people listen to customers talk about the problems they were facing and the suggestions they had for product improvement. We exposed our people to products of competitors by tearing those products apart and analyzing the good and bad and comparing them with our own, thereby making people see why customers buy someone else's products rather than ours.

The patience and confidence that our chairman, Mr. Ratan Tata, displayed toward the entire management—simultaneously exhorting them to stretch themselves—ensured that the organization, though depressed, did not lose its confidence.

McKinsey: *You mentioned colleagues with experience. Were they the most resistant?*

Ravi Kant: The most frozen layer in any organization, I think, is the people with experience who think they know best, who believe that nothing can be changed, and who typically exhibit a not-invented-here syndrome. When we started to connect with what we call the younger high performers, on the other hand—people in their late 20s and early 30s—it was very different. We would have breakfast meetings with a dozen of them, and we would invite them to give very, very frank views. We soon realized that they were suffocated and that they wanted change. So we started picking out some of these individuals and giving them challenges.

In fact, the whole cost initiative came from one of the breakfast meetings at our operation in Pune. Everyone had been talking about cost reductions and thinking in terms of one-half of a percent or 1 percent, but these young employees indicated that they thought a target of 10 percent was possible. They were all from different disciplines, so I said to them during the meeting, "I am in Pune for the next four hours, and I want you all to get together now as a team; I don't want you to go back to work. But before I leave, I want you to make a presentation on how it can be done."

We then made the senior people sit in on the presentation, and it quickly became clear that our 10 percent target was indeed achievable. After this, we urged the young employees to put together a bigger team from Jamshedpur and Lucknow, to include representatives from sales and marketing, and to spend ten days working on the plan. That was the defining moment. If we had tried to go only through the top, we might not have succeeded as well, and the transformation might have taken much longer.

McKinsey: *So were these young people acting as role models?*

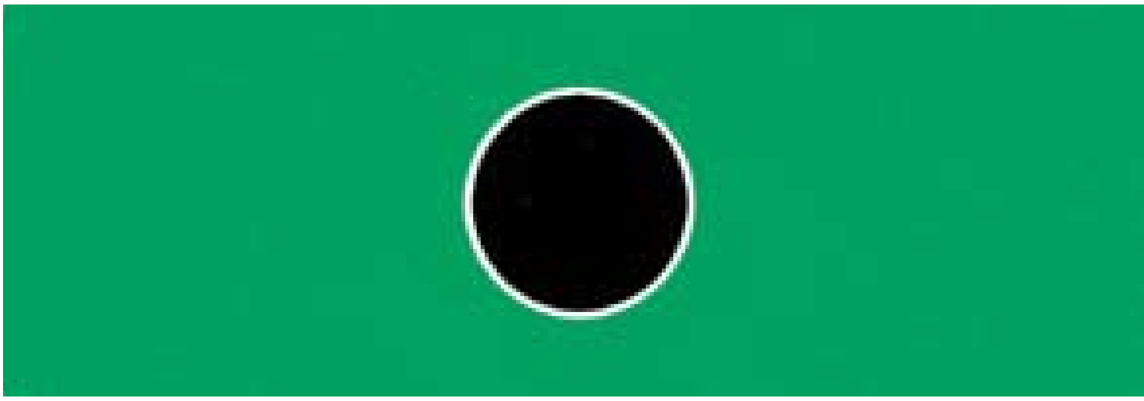
Ravi Kant: Yes, in a way. As a means of accelerating change, we identified individuals who would serve as examples to others. For example, I asked one young person if he would take over our new small-truck project. I had to sell the idea to him and encourage him to take the risk. As things turned out, the project became a phenomenal success and he did a fantastic job. A lot of other young people now want to take on this sort of challenge. Now people are saying that if you respond to challenges and take risks, you can cut through the hierarchy and rise up in the organization.

McKinsey: *How did you sustain the energy needed to continue the transformation beyond the initial phase?*

Ravi Kant: After the initial two-year phase, during which we turned the 5 billion rupee loss into a 5 billion rupee profit, we found that further cost reductions were not forthcoming. The feeling was that there was little scope to do more. At this point, we injected new discipline, put back on the table difficult ideas that earlier had been considered and dropped, and renewed our determination to go for further cost reductions. This became especially important as commodity prices were going through the roof. Steel moved up by 50 to 70 percent, followed by nonferrous metals, rubber, and tires, driven in large part by Chinese consumption. This put us somewhat on the back foot, and our breakeven crept back up to 40 percent, from the 33 percent of capacity utilization that we had earlier achieved. We were able to partially offset that increase by the cost reductions, partially by a mild revision in prices, and partially by taking a 1 to 1.5 percent hit on our EBITDA[1] margins.

In phase two we did several very important things. Apart from reducing the breakeven, we worked very hard on reducing the impact of our cyclical business. We found that the market was not homogeneous; heavy vehicles were very cyclical, light ones less so, and buses hardly at all, since 60 percent of purchases were made by state governments. So we decided to increase our exposure to light vehicles, buses, and nonvehicle businesses like spare parts and maintenance contracts and to set up separate lines in the marketing department for all of them. This helped sharpen our focus on individual customer categories and facilitated a tailored approach to each one, given that the competition in each case was different.

Despite initial hiccups, we succeeded in establishing a strong presence in the car market through the launch of the Indica hatchback, followed by the Indigo sedan and the station wagon. Today we are the second-largest manufacturer of passenger vehicles in India. This



has been achieved in an environment of intense competition with most well-known brands in the world.

McKinsey: *Can you tell us why international diversification was such a key part of the transformation strategy?*

Ravi Kant: It was all part of, first, reducing the impact of domestic cyclicality—cyclicality is present across the world but in different phases in different places—and, second, seeking new geographies for growth in the face of the limitations of the domestic market, especially in commercial vehicles, where we enjoy a very high market share of over 60 percent. If you have market-leading products, you can leverage them internationally. By identifying about 12 countries as priority markets, rather than the 60 to 70 countries we were trying to tap previously, we have grown our international sales to some 50,000 vehicles, against 7,000 to 8,000 four years ago.

McKinsey: *As the leader of a major transformation, what have you found to be the biggest challenge?*

Ravi Kant: The speed of change is increasing very substantially, and the fact that we are still not able to exceed that rate is certainly a cause for concern. We still have a lot of catching up to do, and therefore we need to work on a response time such that we accelerate our speed. We are riding high at the moment because the market is in a growth phase, but I am cautioning everybody not to be complacent. A lot of our success is due to a favorable environment. What would happen if the environment turned against us tomorrow, which certainly could happen in a cyclical industry? We should assume we are already in a crisis situation and therefore look at things from that perspective.

In a broad way, Tata Motors has been silently transforming itself for a long time—and this will continue. The company started manufacturing locomotives, then concentrated on heavy trucks before moving to light trucks, multi-utility vehicles, passenger cars, and buses. We continually have to reinvent ourselves. We should see ourselves as being in the business of providing transport solutions. The important thing is to keep looking at external changes in the marketplace and to respond to these changes appropriately while continuing to retain our values, which have been our beacon for the past 60 years. Tata Motors used to be an engineer's organization that needed to understand more about profits, costs, and contributions. Now people at all levels realize it doesn't make sense to just manufacture anything, that products must sell to make a healthy contribution, and that market share must continually be increased to sustain growth.

McKinsey: *Do you see people as a constraining factor?*

Ravi Kant: No and yes. No because we have one of the strongest pools of competent people any organization in the country could have. Yes because we need to have an even larger pool to meet the challenging objectives we have set for ourselves.

McKinsey: *What aspirations are you setting to keep the momentum going in the year ahead?*

Ravi Kant: We want to see ourselves as one of the most respected companies not only in the automobile industry but also in India's economy as a whole. Of course, we want to grow and produce a healthy bottom line, necessary for sustained growth. But in doing so, we want to be seen as an innovative company breaking new ground and going into uncharted territories successfully. Finally, we want to achieve this the Tata way—transparently, ethically, and meeting our corporate social responsibility. We want to make India proud.

[1] Earnings before interest, taxes, depreciation, and amortization.

Gautam Kumra is a director in McKinsey's Delhi office.